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European Review

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24 October 1986

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European Review

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Economic News in Brief

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Some articles are preliminary views of a subject or speculative, but the contents normally will be coordinated as appropriate with other offices within CIA. Occasionally an article will represent the views of a single analyst; these items will be designated as uncoordinated views.

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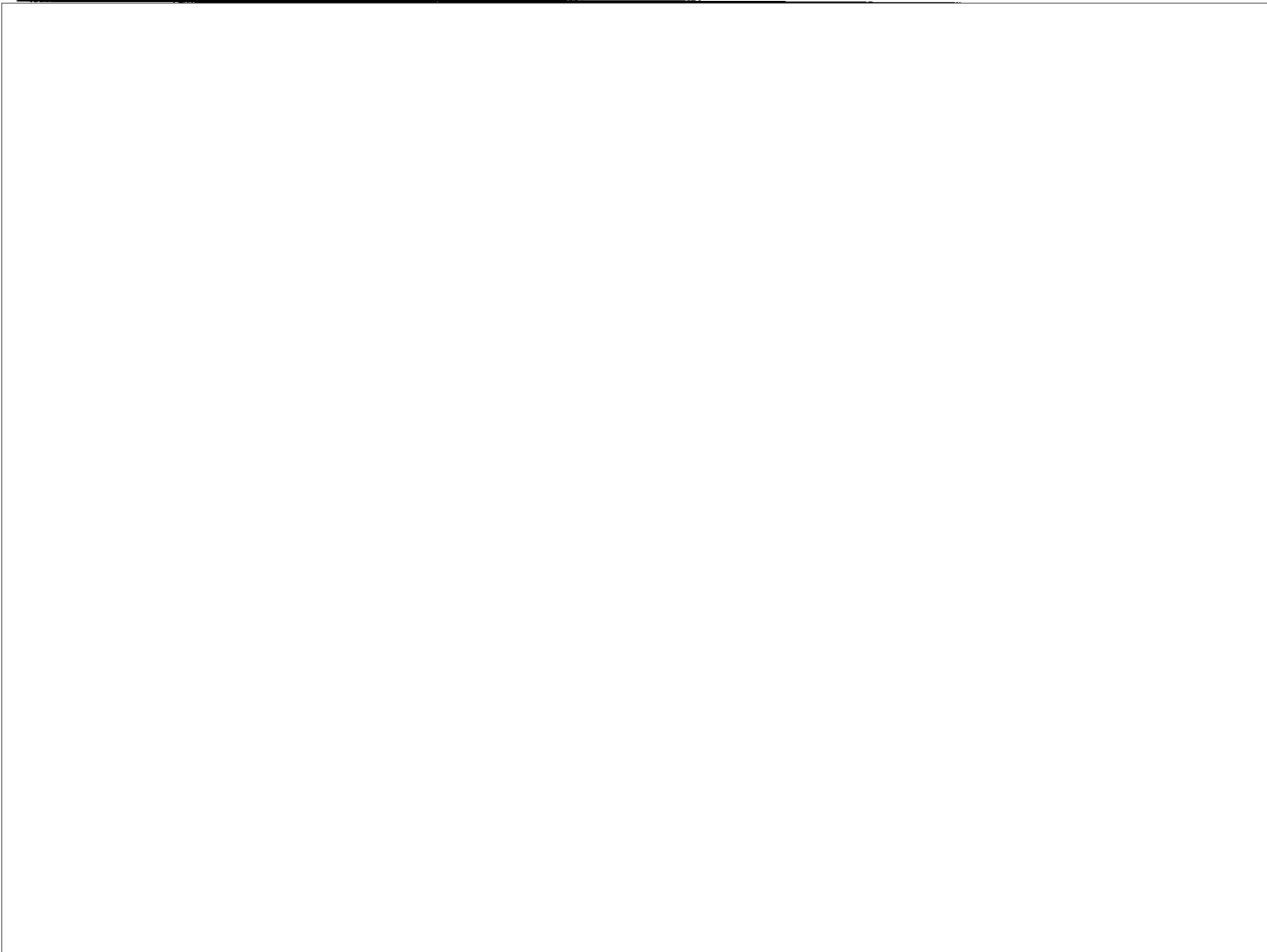
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European Review

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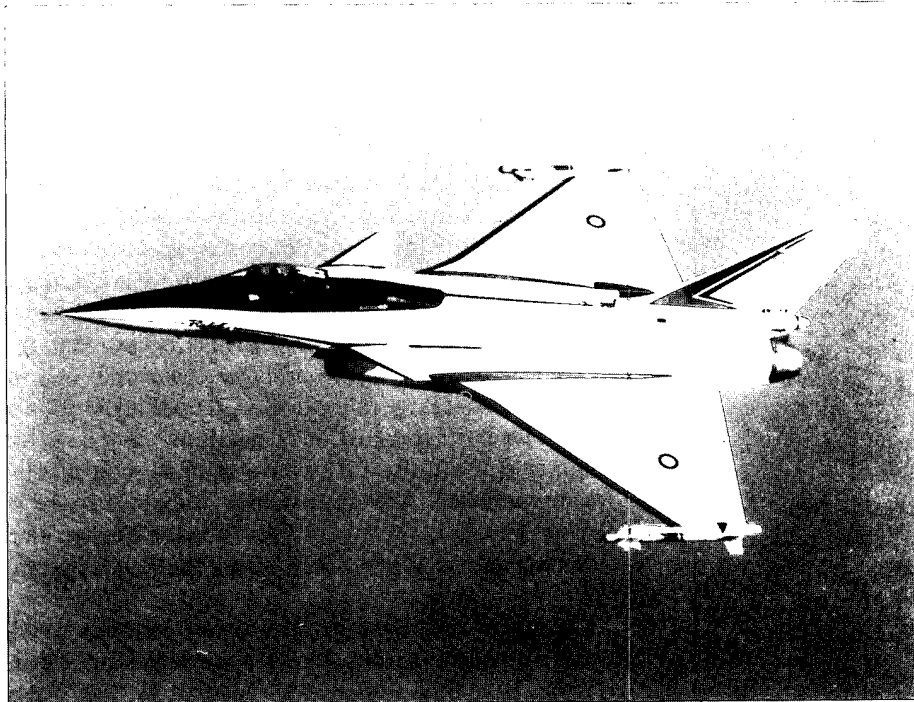
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France

US Engines for the Rafale Fighter [REDACTED]

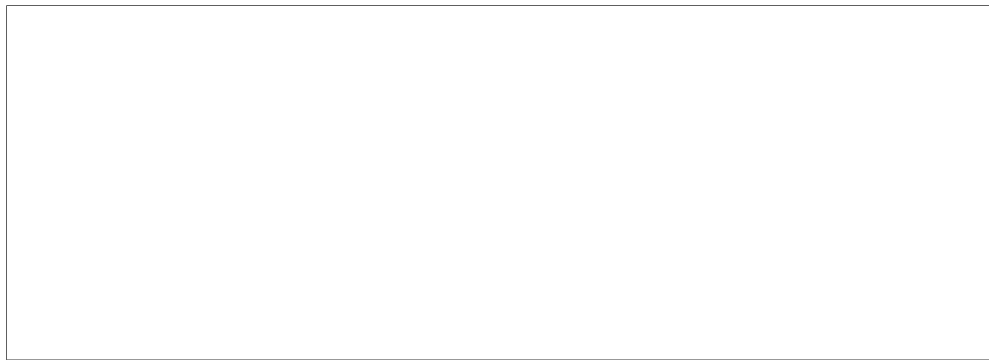
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France's Rafale at the Farnborough Air Show [REDACTED]

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[REDACTED]

Dassault-Breguet has been actively seeking partners to cooperate in the development of the Rafale. Generally reliable press reports indicate that the French have discussed the possibility of building the new-generation fighter as a multinational venture with senior defense officials from Belgium, Denmark, Norway, and the Netherlands. [REDACTED]

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There are also indications that Dassault-Breguet may now be looking outside

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Europe in hopes of obtaining additional partners. []

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[]—who reportedly will retire this month to assume a senior post with Dassault-Breguet—favors US-French cooperation, particularly in engine and radar development. []

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The F-404 engine, which is also used in the US-built F-18, is probably more powerful than the M-88 Mk.1 currently being developed by SNECMA for the Rafale. The ability to fit either engine in the new fighter and allow potential buyers a choice should make the Rafale competitive on the export market. Much depends on the success of the M-88, now in the prototype stage, and the ability of France and the United States to agree on terms. At the same time, France's decision to build a naval version of the new fighter probably precludes the sale of F-18s to France. The F-18, currently in service with the US Navy and the Marine Corps—as well as in Canada, Australia, and recently purchased by Spain—has been favored by the French Navy to replace its aging US-built F-8s and Super Entendards on the new nuclear-powered aircraft carrier. The final go-ahead for the production of approximately 330 aircraft for the French Air Force and Navy is currently awaiting approval under the military programs law. The Rafale is expected to be operational in the mid-1990s, and Dassault-Breguet sees a potential worldwide market for approximately 1,000 aircraft. []

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Spain-United States

Madrid's Stance on Base Talks []

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Spanish leaders may be willing to consider substantial concessions in bilateral talks on the US bases despite Defense Minister Serra's recent tough statements. Serra argued vigorously to a US official that Spain's decision to remain in NATO in the March referendum should lead to negotiation of a "drastic reduction" in US forces in Spain through the bilateral base talks. He warned that, if the talks did not succeed within the next year, the United States would have to negotiate an entirely new bilateral agreement. Serra added that he was prepared to come to Washington to discuss the base issue with Secretary Weinberger once the current negotiations were further along. Spanish leaders want a substantial reduction of US forces, but they probably have not decided on their minimum objectives in the talks, and they may be trying to see how much they can get with a tough initial position. []

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Prime Minister Gonzalez wants to maintain what he views as his newly acquired status as a Western leader and probably will try to avoid jeopardizing that position by pressing Washington too hard. Last spring one of his senior aides raised with a US official the possibility of moving US operations at Torrejon Airbase to another location in Spain. The gap between that scenario and the official Spanish position that US forces at Torrejon, Zaragoza, and Moron must leave Spain altogether suggests that Spanish leaders might eventually be willing to settle for much less than they are asking. Serra's apparent hope of negotiating directly with Secretary Weinberger may indicate, however, that Spain will not yield much ground before raising the issue to a high level. Gonzalez's considerable pride may still make it hard for him to back down unless he believes US leaders have taken his

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negotiating position seriously and until he is convinced he has received enough cosmetic adjustments to save face with the Spanish electorate. [REDACTED]

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[REDACTED]

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Finland-Sweden**Joint Naval Exercises** [REDACTED]

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[REDACTED] appears to substantiate previously rumored—but never confirmed—peacetime cooperation between the Finnish and Swedish Navies. [REDACTED] the two navies conduct joint antisubmarine exercises on a routine basis when their ships visit each other's ports [REDACTED] may well be using frequent visits with his Swedish counterpart to coordinate the exercise activity. [REDACTED] US Navy personnel learned in May 1986 that the Finnish Navy had tested some of its new shipboard and underwater ASW systems against "friendly"—presumably Swedish—submarines.

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[REDACTED]

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Although Finnish-Swedish military cooperation has been suspected for some time, these reports provide the first firm indications of joint naval training operations. Because neither country normally trains with other nations' forces, joint exercises would provide both the Swedish and Finnish Navies a rare opportunity to evaluate their effectiveness against other forces. Since Finland has no submarines, it would particularly benefit from the opportunity to test its ASW capability [REDACTED]

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**Czechoslovakia–
West Germany–Austria****Border Incidents** [REDACTED]

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Recent actions by Czechoslovak border guards against West German and Austrian citizens have angered both Bonn and Vienna, causing a temporary cooling of relations between Prague and its Western neighbors. In the most serious and bizarre incident, Czechoslovak gunfire last month killed a retired Bundeswehr colonel on West German territory. According to Czechoslovak accounts, border guards shot him by mistake when firing on two Poles trying to escape across the border. Prague claims he died en route to a hospital in Czechoslovakia. The regime formally apologized to Bonn and returned the body a few days later. The incident might then have blown over quickly but for the discovery that the body was missing parts apparently damaged by the bullets. Both West German politicians and the media were outraged at this "body snatching." The Kohl government demanded a complete explanation of the incident and has proposed formation of a joint commission of inquiry. Foreign Minister Genscher expressed his country's anger to Czechoslovak Foreign Minister Chnoupek during their meeting at the United Nations. [REDACTED]

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The Austrians have also issued sharp protests over recent Czechoslovak actions. Shortly after the West German incident, Czechoslovak troops apparently crossed into Austrian territory to apprehend an old man who was gathering mushrooms.

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One day later, Czechoslovak border officials turned back an Austrian professor who was leading a delegation to Prague, presumably because of his rightwing reputation. These actions ironically followed a meeting of the Czechoslovak-Austrian committee on border incidents at which both sides agreed the situation was good. To mark its displeasure, Vienna canceled the visit of a midlevel politician to Prague and Foreign Minister Jankowitsch sharply chastised the Czechoslovaks for their actions.

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These incidents have clearly hurt relations between Czechoslovakia and its two Western neighbors, but, serious as they are, they are unlikely to cause lasting damage. Relations have been improving slowly in recent years, and all sides are interested in maintaining the momentum. The Czechoslovaks especially want to increase trade, and the Austrians and West Germans see major political benefits in pursuing dialogue with the East. Similar border incidents in the past, including killings, have had little lasting impact on relations. Austria and West Germany have been willing to overlook such mishaps and are likely to soon forget these incidents as well.

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East Germany- West Berlin

Initiative on Berlin Anniversary

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East German leader Erich Honecker may again be probing the status of Berlin by inviting West Berlin Governing Mayor Diepgen to two ceremonies in the East celebrating Berlin's 750th anniversary in October 1987. Planning for the yearlong festivities, important to both halves of the city, has been a source of contention as the East Germans have sought to use them to bolster the status of their "capital" in the heart of old Berlin. The series of ceremonies next year will give the East plenty of opportunity for mischief and presents the occupying Allies, the West German Government, and the West Berlin Senat with delicate new problems.

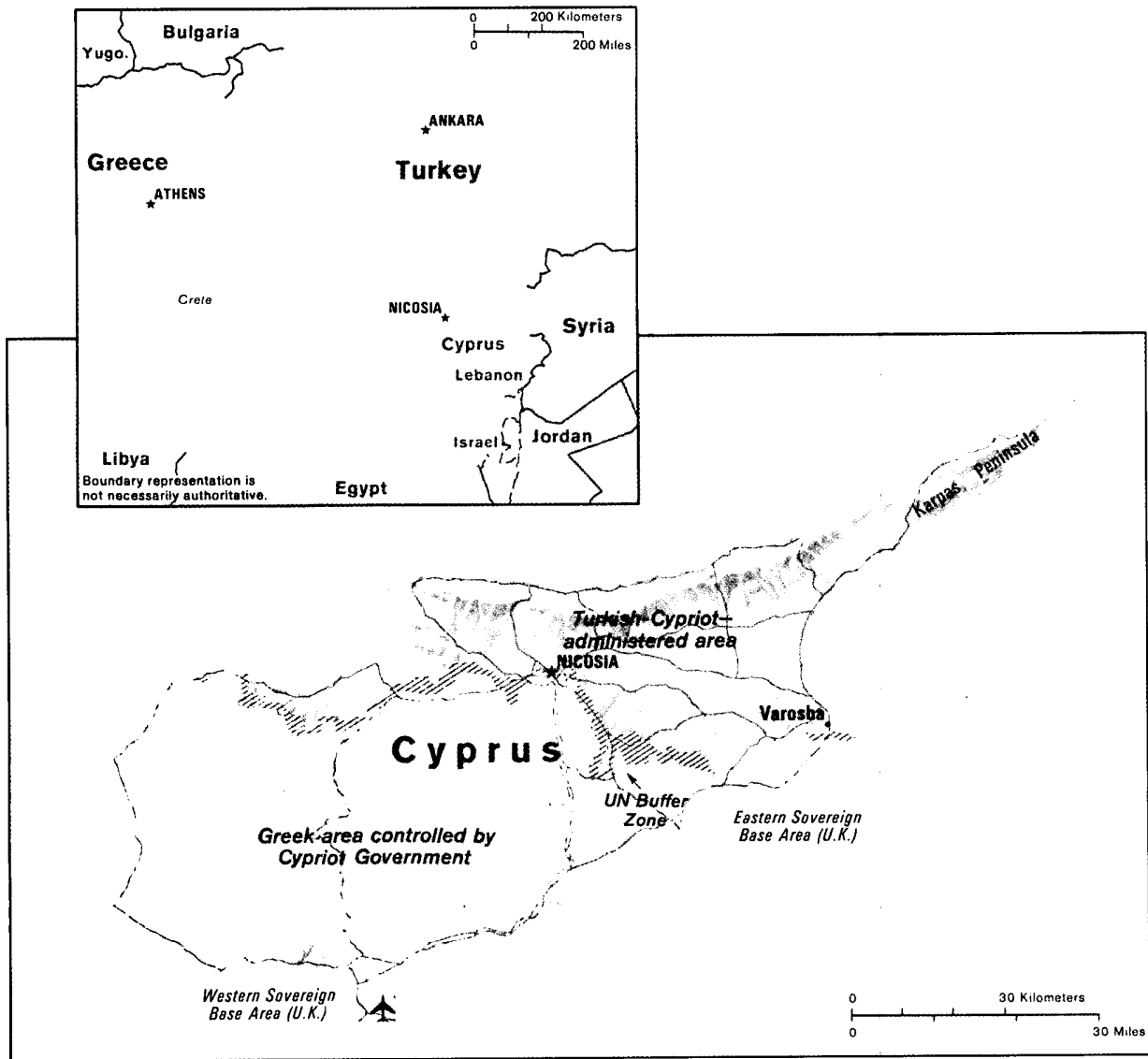
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Diepgen almost certainly would like to accept at least one of the invitations. He is sensitive to Allied concerns that the East Germans may use the ceremonies to highlight their views of East Berlin's status, perhaps by including military parades or references to the "capital of the GDR." At the same time, Diepgen actively is seeking opportunities to expand contacts with the East, which are increasingly popular in West Berlin. If the Allies strongly press Diepgen not to accept the invitations, he might be willing to suggest to East Berlin that he attend a less overtly political ceremony instead. The Social Democrats and Alternatives, however, would loudly accuse the Allies of obstructing West Berlin's dialogue with the East if their pressure became public.

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Articles

**Cyprus: What If United Nations
Negotiations Fail?**

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The United Nations effort to bring about a negotiated settlement on Cyprus through the good offices of UN Secretary General Perez de Cuellar appears to be at an impasse. The Greek Cypriot refusal in June to accept his painfully constructed third draft "framework" agreement as a basis for negotiations, and the subsequent Turkish Cypriot refusal to consider any modifications in that document, bode ill for the UN effort. There is broad international support for keeping the UN effort alive, however, and Perez de Cuellar may still devise a formula for resurrecting his initiative or an alternative approach.

If the path toward a negotiated settlement remains blocked, a number of unsettling developments appear probable. These include:

- An intensified effort by the Turks and Turkish Cypriots to consolidate the independent status of northern Cyprus and win recognition from third countries.
- A flurry of diplomatic activity by the Greeks and Greek Cypriots aimed at heightening international attention to the Cyprus dispute, blocking Turkish Cypriot state-building efforts, and undermining Turkey's improved image in Western Europe.
- Increased opportunities for Soviet involvement in the region.
- Pressure from the Greeks and Greek Cypriots for more direct US support and countervailing pressure from Ankara.

Any of these courses of action could dangerously increase tensions in a region of major strategic importance to the United States.

Background

The current UN effort to achieve a comprehensive Cyprus settlement began in August 1984. Since then the United Nations has been trying to create an acceptable "framework" for negotiations between the Greek and Turkish Cypriots. In January 1985, a UN-sponsored summit meeting broke down when the Greek Cypriot side maintained it had come only to discuss the UN's initial draft agreement, while the Turkish Cypriots insisted on its formal acceptance. In April 1985, the UN came up with a revised version that the Greek Cypriots accepted and the Turkish Cypriots rejected. Following protracted discussions with both sides, the UN Secretary General produced yet another agreement last March. The Turkish Cypriots have accepted this document, but the Greek Cypriots for all practical purposes have rejected it.

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Possible Turkish Cypriot Moves

We believe prolongation of the current impasse—and the widespread perception that Greek Cypriot obstinacy is responsible for it—will encourage the Turkish Cypriots to take steps to legitimize their claim to the 37 percent of the island they control—the so-called Turkish Republic of Northern Cyprus (TRNC). There is precedent for such action. After gaining the diplomatic high ground at the January 1985 summit, Turkish Cypriot leader Denktash used the favorable international climate to strengthen his "state" by promulgating a new constitution and calling presidential and parliamentary elections.

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Denktash could well be tempted to use Greek Cypriot rejection of the third UN draft agreement to justify

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further state-building efforts. He has already indirectly challenged the status of UN forces on Cyprus. When he closed the border with southern Cyprus for a week in early July, he presented it not as retaliation for a similar Greek Cypriot action in protest of Turkish Prime Minister Ozal's visit to northern Cyprus, but as a demonstration of Turkish Cypriot sovereignty over the north. The Turkish Cypriot Council of Ministers reiterated this point when it reopened the border, alleging that Turkish Cypriot "sovereignty" had been demonstrated to the world. []

The border closing, moreover, succeeded in extracting tacit UN acknowledgment of the Denktash regime's authority over the north. Only after prolonged negotiations was the United Nations able to persuade Denktash to give up his demands for visas from all travelers from the south and for formal talks with the UN on an agreement fixing the conditions for the future movement of UNFICYP¹ forces in the Turkish zone. On the basis of Denktash's past practices, it would be typical for him to use these negotiations as confirmation of the TRNC's "sovereignty" and to push the process further with other restrictions on UN troop movements. []

There also is evidence that the Turkish Cypriots may be considering more direct steps to consolidate their "state." Over the past year Denktash has periodically dropped hints about issuing a Turkish currency, opening airlinks, or establishing commercial and cultural ties to third countries as steps toward attaining full diplomatic recognition. In addition to these moves, we believe he might be seriously considering resettling the deserted city of Varosha. He has been quoted in the Turkish press as saying that no one should be surprised if Varosha were to be resettled. US Embassy reporting indicates that British

¹ UNFICYP (United Nations Force in Cyprus) was founded in 1964 for a three-month period—later extended by successive resolutions in the UN Security Council—to keep the peace between the Greek and Turkish Cypriot communities pending resolution of the outstanding issues between them. It is composed of some 2,000 men from seven countries—Austria, Canada, Denmark, Finland, Iceland, Sweden, and the United Kingdom. []

citizens with property in Varosha have been told to register their interests with the Turkish Cypriot authorities or risk forfeiting their claims.² []

View from Ankara

Ankara has traditionally exercised some restraint on Denktash's state-building efforts. There are indications, for example, that Denktash's past willingness to cooperate with UN peace efforts were, at least in part, because of pressure from Ankara. Ankara's role could change, however, if Turkish officials perceive that the negotiations are failing. []

In fact, Turkish actions and public statements suggest that Ankara already is edging toward a tougher policy—despite assurances to Washington to the contrary. During Prime Minister Ozal's visit to northern Cyprus, for example, he made a number of statements supporting Turkish Cypriot "equality" with the Greek Cypriots and endorsed Denktash's state-building efforts. Ozal reportedly was also directly involved in orchestrating Turkish Cypriot actions on the border; []

[] Press reports indicate that the Turks have recently been sounding out various Islamic countries regarding the establishment of cultural, educational, athletic, and trade relations for the purpose of gradually upgrading the TRNC's international status. []

Reports that Ankara has increased Turkish military strength on Cyprus may be another indication that Ankara is positioning itself for possible new moves on the island. We believe Ankara recently shipped an unknown number of M48-A5 tanks to northern Cyprus. The M48-A5 has a larger gun, an improved fire-control system, and a better engine than the older M-47 and M-48 tanks currently on the island.

² Varosha has long been a focal point in the intercommunal talks. Until the 1974 Turkish intervention, it was a prosperous resort town largely populated by Greek Cypriots. It is currently unoccupied and under UNFICYP's jurisdiction. []

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[] 5,000 Turkish troops were to be added to the forces in northern Cyprus this summer in conjunction with annual troop rotation. A 5,000-man increase in Turkish troop strength—from about 20,000 to 25,000 troops—would be the largest single jump since the Turkish intervention in 1974. These increases in Turkish force levels would enhance Ankara's ability to deter Greek Cypriot or Greek reactions to new Turkish Cypriot political moves, but they could also start an arms race on the island. []

Whether Ankara decides to support new Turkish Cypriot moves depends on a variety of factors. One clearly is the status of the UN peace effort. If it withers—and the responsibility can be convincingly attributed to Greek Cypriot obstinacy—Ankara would have a plausible justification for giving Denktash the go-ahead. On the other hand, the Turks have more to consider than just the interests of Turkish Cypriots—they have to factor in the effect Turkish Cypriot actions will have on military aid deliberations in Washington. These considerations suggest that if the Turks decide to give Denktash the green light on Cyprus, they will wait until late fall when the prospects for the UN peace effort also will be clearer. []

Greek and Greek Cypriot Reactions

Unlike the Turks, the Greek Cypriots lack the ability to revise the status quo unilaterally in their favor. Their only possibility of altering the situation remains a negotiated settlement, and at present they appear to hope that their roadblock to the Secretary General's peace effort will force the UN to come up with a new approach that will be more in their favor. If Perez de Cuellar fails and no acceptable alternative develops, both Athens and Nicosia are likely to react by launching a major diplomatic offensive aimed at rallying international sentiment in their favor and against Turkish Cypriot state-building efforts. Nicosia is already stepping up pressure on the United States, the United Nations, and the European Community (EC) by warning in the press and UN forums that Denktash may be preparing to challenge the status quo. In addition, Nicosia has sent special emissaries and letters explaining why the latest UN proposal is "unworkable" and encouraging other

countries not to deal with the Turkish Cypriots. The Greeks have also tried to use the recent border closing incident as ammunition against Turkey in the EC. []

If the Turkish Cypriots were to alter seriously the status quo—for example, by resettling Varosha—the Greek Cypriots would undoubtedly go to the United Nations. Athens for its part would almost certainly try to muster support for political and economic sanctions against Turkey in the EC and NATO. Both Nicosia and Athens would press Washington to become more directly involved. The United States would then have to choose between supporting one NATO ally and outraging the other or staying neutral and irritating both. []

In response to Turkish Cypriot initiatives, the Greek side might resort to unilateral actions constituting a more serious threat to peace. The possibilities include building up the Greek Cypriot forces, increasing the Greek military presence on Cyprus, and partially or completely cutting off Turkish Cypriot access to essential supplies of water and electricity from the south. Any of these actions would require a Turkish response, significantly raising the risk of a military conflict on the island. []

Increased Opportunity for Soviet Activity

A prolonged hiatus in UN efforts to mediate a solution to the issue would present the Soviets with new opportunities to promote their own solutions to the problem. There are indications that Moscow is already moving to play more actively in the Cyprus problem. They have tabled a proposal for an international conference that would, of course, include the USSR. Moscow's goal is to promote an agreement for a nonaligned, demilitarized island—one that would entail removing the British Sovereign Base areas. Greek Cypriot leader Kyprianou is not above playing along with the idea to prod Washington into playing a more direct role, even though Nicosia does not want Moscow to be directly involved in Cypriot affairs. []

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The Soviets have been pushing the idea of an international conference more vigorously since the breakdown of the UN effort. We have seen a flurry of Soviet diplomatic activity on the island to discuss the proposal, and Moscow has named a younger and more vigorous ambassador with a strong background in UN affairs to Cyprus. The Soviets also are openly supporting the Greek Cypriot position now, a departure from their past efforts to maintain an evenhanded approach. []

Implications

Unless the peace process can be revived, Cyprus appears headed for eventual partition. The Greek Cypriot responses to the latest UN peace proposal suggest that they may be growing resigned to permanent partition if the alternative is an agreement that would preserve formal unity on Turkish terms. Some Greek Cypriots feel they are better off as they are, controlling their own destiny on a divided island, rather than being exposed to the constant risk of Turkish interference or intervention in a dubiously reunited country. The Turkish Cypriots, for their part, have less to gain from a settlement than the Greek Cypriots. As the international community becomes increasingly used to the existence of the "Turkish Republic of Northern Cyprus," the Turkish Cypriots will move closer and closer to achieving their goal of establishing an independent state without a settlement. []

Over the long haul, all the players in the Cyprus problem—even Athens and Nicosia—may come to see partition as the only possible solution, even though the Greek side will be extremely reluctant to acknowledge it openly. In the short term, however, the process of transition, if it takes place, is likely to be fraught with danger. Greek Cypriots are likely to respond to any unilateral Turkish efforts to consolidate their state with actions of their own. The possibilities open to them—running the gamut from "internationalizing" the issue to military moves—would lead a region of major strategic importance to the United States into a new phase of dangerous tensions. []

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Austria: Back Together Again

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Austrians may soon see a renewal of the same partnership that ruled the country from 1947 to 1965. Current opinion polls place both the Socialist and People's Parties below 50 percent of the vote, and the leaders of these parties have come out strongly in favor of a grand coalition if the voters do, in fact, fail to award either party a majority on 23 November. At this point, such a government promises to be not only stable, but, more important, it is likely to have the broad support necessary to push through badly needed economic reforms.

The Freedom Party Moves Right

Since 1983, Austria has been governed by a coalition of the Socialist and Freedom Parties—a union that had been inconceivable only a few years earlier. For much of its history, the Freedom Party (FPOe) served as a repository for this Alpine country's shrinking pool of Pan-Germanists, some of them veterans of the Third Reich. At the same time, however, the party has espoused economic tenets that place it close to mainstream European liberalism. Finally, as a perennial party of opposition, the FPOe has also attracted protest voters regardless of cause.

In recent years, the liberal wing has been preeminent, at least at the national level. Under the leadership of Chairman Norbert Steger, the FPOe has stressed such liberal themes as reducing the state's role in the economy and ending the use of nuclear energy. So positioned, the Freedom Party was able to join the Socialists (SPOe) in a social/liberal coalition when the Socialists lost their parliamentary majority in 1983. This was the FPOe's first opportunity to exercise power at the federal level.

The nationalists have not remained quiescent, however, and the declining popularity of both the coalition and the Freedom Party has given them openings to attack the liberal leadership. These openings have also provided a welcome excuse for the brash young leader of the party's Carinthian chapter, Joerg Haider, to promote his own fortunes by making

himself spokesman for the nationalists. During the last three years, Haider has launched repeated assaults on the party's direction and on Steger's performance as chairman; the most recent challenge came in May, when Haider used Steger's appointment of Helmut Kruenes as Austria's new Defense Minister to justify renewed demands for a change in party leadership. Haider lost that battle, but he won the war in September, when he captured 57.7 percent of the votes for chairman to Steger's 39.2 percent.

It is not entirely clear why the delegates elevated Haider over Steger. The Socialists had hinted before the convention that such a move would bring about the end of the coalition—and this at a time when the polls showed declining support for both the government and the FPOe. Yet, it may have been precisely these poll results that inspired the party rank and file—never strongly enamored of Steger as a personality in the first place—to replace the chairman. Indeed,

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many delegates objected not so much to the party's performance in the coalition as to the leadership's inability to sell the party's role and accomplishments to the public. Some may also have reasoned that the election of Kurt Waldheim as Federal President in June proves that there exists a sizable nationalist vote in Austria, while others may have surmised that an end to the FPOe's part in the government would bring back many of the protest votes the party appears to have lost since 1983.

The Socialists React

Whatever the reasons, the Socialist leadership quickly made it known that the SPOe could no longer work with the Freedom Party. Immediately after the vote in Innsbruck, Chancellor Vranitzky called a new national election for November, five months before the scheduled vote in April. Vranitzky justified his action by pointing out that the coalition had been

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negotiated in 1983 with a Freedom Party in which the liberal wing was dominant; Haider's election, however, showed this no longer to be the case. The suddenness of the move caught many observers by surprise. The Socialists had spent much of the summer rejecting calls from the opposition for an early election, and it was generally assumed that the Socialists wished to give the popular and respected Vranitzky time to win his laurels as Chancellor before testing the government's and the SPOe's popularity at the polls. In retrospect, however, the elevation of Haider left Vranitzky with little choice. The left wing of the party almost certainly would have displayed little patience for a coalition with a Freedom Party led by Haider, and Vranitzky probably did not relish the prospect of a five-month partnership.

Vranitzky received high marks, initially at least, for having moved decisively to call a new election and to show concern for preserving his party's claim to be the chief defender of the country's postwar antifascist legacy. Many Socialists, recognizing that the Chancellor is now their party's best electoral asset, have probably been encouraged by this favorable response.

Outlook: A Grand Coalition

It is doubtful that Vranitzky's calculated gamble will be enough to win a majority—or even a plurality—for the Socialists. Voter dissatisfaction with the SPOe, which has ruled Austria since 1970, is high. For example, most observers attribute Waldheim's victory in June—the first ever by a non-Socialist candidate for President—primarily to this voter alienation. And the Socialists lost approximately 5 percentage points in the provincial election in Styria in late September. In addition, polls placed the Socialists a few percentage points behind the conservative People's Party (OeVP), 44 to 46 percent, in July.

This does not mean, of course, that the Socialists are bound to lose on 23 November. Vranitzky's image as a competent tactician has kept his personal popularity high. One poll recently gave the Chancellor an approval rating of 57 percent, and, in fact, 24 percent of those who identified themselves as People's Party voters claimed that they would give their votes to a Socialist ticket led by Vranitzky.

Vranitzky's popularity notwithstanding, it seems likely that neither of the two parties will win a majority, and, in this event, a grand coalition remains the most likely outcome. Vranitzky, seconded by his party's Executive Committee, has already expressed his preference for such a government. Leading figures in the People's Party also favor a grand coalition, among them chairman and chancellor-candidate Alois Mock.

No Spoiler on the Horizon

We do not believe that any of the smaller parties can play a spoiler role in this election. At the moment, the Freedom Party is polling less than 4 percent—3.5 in July—and may not have the votes to build a government in November. The Socialists have already shown their dislike for an FPOe led by Haider. Moreover, the current animosity between the FPOe and OeVP is well documented. The last three years have witnessed numerous hostile exchanges between the parties' leaders, and even Haider dismissed the possibility of an FPOe/OeVP coalition at the congress in Innsbruck. Some in the two parties may believe that the nationalist sentiment awakened during the presidential election campaign is strong enough to support such a coalition, but, in our view, they remain a distinct minority.

The Greens, as always, are an enigma. Polls currently give them about 6.5 percent of the vote, and there is no doubt that enough potential Green voters exist to put Green deputies in the Nationalrat. The question for the Greens is whether they will have a unified ticket that can capture those votes. In 1983, separate environmental and alternative groups competed for the Green vote, and, until recently, the divisions and acrimony persisted. This July, however, leaders of three factions agreed to unite their groups for the federal election, and in September leaders of five factions decided to field a joint list for the election. A party congress is planned for October to elect leaders and select candidates. Whether the newfound unity will persist until 23 November remains to be seen. In any event, Green leaders have declared that all the

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other parties are unworthy of their cooperation, and the Greens' impact will depend on the ability to attract voters from the other camps, principally from the Socialists.

Tackling Tough Economic Problems

A Socialist-People's Party coalition may be just what the country needs in November. To be sure, there have been problems in Austria's past experiences with a grand coalition. This was the partnership, for example, that established the proportional system of appointments to the managing boards of the nationalized industries in the early years of the Second Republic. This politicization, many observers conclude, has contributed markedly to the poor state of affairs in which those industries find themselves today. And numerous critics point out that contemporary Austria is very different from the postwar society those grand coalitions ruled so effectively.

There are, however, potentially important advantages in a grand coalition at this time. In the first place, it promises to be relatively stable, despite what one might expect when leftist and conservative parties combine. There are several reasons for this. Because the two parties governed together from 1947 to 1965, they have considerable experience working together. In addition, the leadership of moderates like Mock and Vranitzky suggests that compromises can be reached.

More important, a grand coalition promises to have the broad support necessary to affect badly needed economic reforms. The country's nationalized industries suffer from overproduction, a lack of profits to finance modernization, and they are no longer competitive in international markets. Restructuring will require the cooperation of industry and labor behind the leadership of their respective parties—the OeVP and the SPOe—to bring about changes,

including such measures as limited privatization, an end to subsidies, and politically painful layoffs. The need to reduce the budget deficit and to reform the tax system in order to promote greater investment will also require difficult political decisions, which a grand coalition would find easier to make and enforce. In conversations with US diplomats, many Austrian officials appear to realize that unless these difficult choices are made, the Austrian economy faces rising unemployment and inflation, a dearth of investment capital, and declining export markets.

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Canada: Tories Reopen Parliament

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In reopening Parliament earlier this month, the Tories stressed fiscal responsibility and played down US-Canadian relations. Early media reaction indicates Prime Minister Mulroney will be hard pressed to dispel the perception that the Tories are drifting.

Economic Problems

Ottawa is faced with the likelihood that slow economic growth over the next two years will not allow much deficit reduction or reverse the increasing economic disparities between industrial Ontario and industrial Quebec and the struggling resource-dependent Atlantic and Western provinces. Finance Minister Wilson apparently convinced the Cabinet in August that any relaxation of budgetary restraint would weaken the Canadian dollar and force higher interest rates on the already slowing economy. As a result, the government plans next year only to reallocate existing funds for regional economic development and to establish a federal agency in eastern Canada to coordinate the aid more efficiently.

The Tories hope that proposals for lower personal tax rates will improve their popularity with middle-income voters and add substance to their professions of concern about low-income Canadians.

US Interests

Departing from Mulroney's past strategy, the government deemphasized relations with the United States and stressed themes important to Canadian nationalists. Ottawa played down trade talks with Washington, emphasized GATT instead, and called for improved trade links to Asia. The Tories' reduced emphasis on a bilateral trade pact reflects eroding domestic support for the idea and the intense criticism of Mulroney for his alleged inability to exempt Canada from US protectionism.

Canada's assertion of sovereignty over the Northwest Passage also continues to complicate bilateral relations. In January Ottawa drew formal boundary lines encompassing Arctic claims disputed by

Washington. Earlier this month, the Tories renewed a commitment to build an icebreaker to maintain a presence in Arctic waters. Funds for the ship probably will be pared from defense programs, slowing the already glacial pace of Canadian force modernization.

Tory Tensions

A widening regional split within the Prime Minister's party threatens to sap the government's prestige

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This dispute—and a 21-percent decline in the government's standing in public opinion polls during the past year and a half to September 1986—has aroused the traditionally fractious Conservative caucus. Western alienation was evident in a recent Alberta byelection when the Conservatives barely retained a long-held seat.

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Prospects

The Mulroney government can do little on its own to reverse its political fortunes for the election that is due not later than 1989, but is more likely to occur in 1988. The Conservatives are pinning their hopes on tax reform and US-led economic growth to ease budgetary pressures and reduce unemployment, on demonstrable gains for Canada in trade talks with Washington.

Most of these hopes depend ultimately on decisions largely outside Ottawa's control.

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In the next few years, US domestic and foreign policies are likely to become, more than in the past, convenient scapegoats for the Tories as well as for the opposition.

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Economic News in Brief

Western Europe

Turkey again hinting it may apply for EC membership, possibly as early as December . . . unhappy over lack of progress on EC aid, workers' freedom of movement . . . EC discouraging Ankara, hopes to defer action on membership indefinitely.

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France likely to offer Egypt highly subsidized wheat prices . . . probably will threaten to reduce subsidies on flour sales unless Egypt buys wheat . . . US Embassy says delegation visiting Cairo this month . . . market fifth largest for US exports.

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Spain negotiating to buy Norwegian natural gas for 20 years after production from new fields available in 1992 . . . to reduce dependence on Algeria, Libya . . . Norwegian gas could supply 20 percent of Spain's needs after 1992.

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Eastern Europe

Press reports Hungary activated third reactor at nuclear power plant at Paks . . . plant will generate about one-third of domestic electricity . . . fourth reactor due next year . . . shows commitment to nuclear program despite Chernobyl accident.

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Britain reportedly withdrawing \$50 million export credit guarantee offered Poland in June . . . probably because Warsaw did not make repayment of arrears . . . failure to comply with rescheduling agreements remains obstacle to new government loans.

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